Fiscal Note 2009 Biennium

GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Bill #	HB0598	**Title:**	Distribute certain oil and gas production taxes to cities, towns, and counties
Primary Sponsor:	Erickson, Ron	**Status:**	As Introduced

- ☑ Significant Local Gov Impact
- ☑ Needs to be included in HB 2
- ☑ Technical Concerns
- ☐ Included in the Executive Budget
- ☑ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Expenditures:				
General Fund	$202,134	$91,230	$93,511	$95,849
Revenue:				
General Fund	($1,486,583)	($1,487,514)	($1,488,407)	($1,489,300)
Coal Bed Methane (02)	($20,267)	($20,280)	($20,292)	($20,304)
University Mill Levy (02)	($43,665)	($43,692)	($43,718)	($43,745)
Orphan Share (02)	$1,538,850	$1,539,813	$1,540,737	$1,541,662
Reclamation and Development (02)	$1,538,850	$1,539,813	$1,540,737	$1,541,662
Local Governments	$55,479,109	$55,513,854	$55,547,163	$55,580,491
Net Impact-General Fund Balance:	($1,688,717)	($1,578,744)	($1,581,918)	($1,585,149)

Description of fiscal impact: This legislation shortens the timeframe of the oil and natural gas production tax holiday of taxation at 0.5% to six months for both oil and natural gas. The bill increases the tax on the following six months of production (twelve months for horizontally-completed wells) at 9%. This legislation then distributes the increase in revenues to cities and counties.

FISCAL ANALYSIS

Assumptions:

1. Section 3 of HB 598 shortens the timeframe in which oil and natural gas production qualifies for preferential tax rates to six months. This legislation increases the working interest tax rate after the first six months from 0.5% to 9%. Production would be taxed at the 9% rate for six months (twelve months for horizontally-completed wells); the tax rates after this time period remain the same as current law.

2. In FY 2006, there was $927.9 million in taxable working interest value from qualifying production; $122.1 million of this value occurred in wells taxed as qualifying production for 12 months and $805.8 million of this value occurred in wells taxed as qualifying production for 18 months. Assuming that half of the $122.1 million and one-third of $805.8 million was produced within the first six months, the value that would be subject to the 9% rate under the proposed legislation would be $598.3 million (($927.9 million –($122.1 million/2) – ($805.8 million/3)).
3. This $598.3 million is now taxed at a rate of 0.5% for tax revenues of $2.99 million in FY 2006. HJR 2 revenue assumptions indicate that oil and gas production collections will decrease by 4.05% in FY 2007 and increase by 16.84% in FY 2008 and 0.06% in FY 2009. Assuming all types of production will experience similar growth rates and that the 0.06% growth continues in FY 2010 and FY 2011, the $2.99 million will grow to $3.353 million in FY 2008, $3.355 million in FY 2009, $3.357 in FY 2010, and $3.359 in FY 2011.
4. Under current law, these revenues would be distributed to counties, the coal bed methane account, the reclamation and development account, the orphan share account, the university system levy account, and the general fund. The Legislative Fiscal Division estimates the general fund will receive 44.3318% of these revenues for FY 2008 and FY 2009. Assuming this distribution continues for FY 2010 and FY 2011, the current law collections would be distributed as follows:

Current Law Distribution

	FY 2008	FY 2009	FY 2010	FY 2011
Total Counties (44.3318%)	$1,705,580	$1,706,648	$1,707,672	$1,708,697
General fund (90.22% of state)	$1,486,583	$1,487,514	$1,488,407	$1,489,300
Coal bed methane (1.23% of state)	$20,267	$20,280	$20,292	$20,304
Reclamation and development (2.95% of state)	$48,608	$48,639	$48,668	$48,697
Orphan share (2.95% of state)	$48,608	$48,639	$48,668	$48,697
University system (2.65% of state)	$43,665	$43,692	$43,718	$43,745
Total State (50.3713% of total)	$1,647,731	$1,648,763	$1,649,753	$1,650,742
Total State and Counties	$3,349,041	$3,351,138	$3,353,149	$3,355,161

5. The proposed legislation would tax the $598.3 million of working interest value at 9% for tax revenues of $53.84 million. Growing this revenue according to the HJR 2 revenue assumptions will result in estimated revenues of $60.360 million in FY 2008, $60.397 million in FY 2009, $60.434 million in FY 2010, and $60.470 in FY 2011.
6. Section 5 of HB 598 distributes the full amount of tax revenues from 2.63% to the reclamation and development grants special revenue account, 2.63% to the orphan share account, and the remainder to counties and incorporated cities and towns. This distribution is shown in the table below.

HB 598 Distribution

	FY 2008	FY 2009	FY 2010	FY 2011
2.63% to Reclamation and Development	$1,587,458	$1,588,452	$1,589,405	$1,590,358
2.63% to Orphan Share	$1,587,458	$1,588,452	$1,589,405	$1,590,358
Cities and Counties	$57,184,689	$57,220,502	$57,254,835	$57,289,188
Total	$60,359,604	$60,397,406	$60,433,644	$60,469,905

7. The net effect of the proposed legislation on all of the funds affected is shown in the table below:

Net Effect of Proposed Legislation
(not including expenditures)

	FY2008	**FY2009**	**FY2010**	**FY2011**
General Fund	($1,486,583)	($1,487,514)	($1,488,407)	($1,489,300)
Coal Bed Reclamation	($20,267)	($20,280)	($20,292)	($20,304)
University Levy Account	($43,665)	($43,692)	($43,718)	($43,745)
Cities and Counties	$55,479,109	$55,513,854	$55,547,163	$55,580,491
Reclamation and Development	$1,538,850	$1,539,813	$1,540,737	$1,541,662
Orphan Share	$1,538,850	$1,539,813	$1,540,737	$1,541,662

8. The portion of revenues distributed to cities and counties would be distributed as follows:
   - 40% to each county based on
     - the rural road mileage in each county, as a percent of the total state rural road mileage;
     - the rural population living in the county, as a percent of the rural population in the state; and
     - the land area in the county, as a percent of the total land area of the state.
   - 60% to each incorporated city or town based on
     - the town's population, as a percent of the total state population living in towns; and
     - the town street and alley mileage, as a percent of the state total street and alley mileage.
9. The Department of Revenue will require 1.5 FTE to implement this legislation. One FTE will assist in the development of a new distribution system for these revenues; annually adjust the distribution schedule to counties and cites based on updated road mileage and population; handle all correspondence, data, and questions associated with the distribution; ensure that the appropriate tax rates are applied to the correct wells; and enter production data into computer systems. The half FTE will be an accountant. In addition, $100,000 in contract services is required to develop a new distribution schedule in the Department's computer system. The total administrative costs needed to implement HB 598 would be $203,134 in FY 2008 and $91,230 per year for FY 2009. Expenditures for FY 2010 and FY 2011 have been increased by an inflation factor of 2.5%.

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Fiscal Impact:				
FTE	1.50	1.50	1.50	1.50
Expenditures:				
Personal Services	$79,338	$79,338	$81,321	$83,354
Operating Expenses	$110,996	$11,892	$12,189	$12,494
Equipment	$11,800	$0	$0	$0
TOTAL Expenditures	$202,134	$91,230	$93,511	$95,849
Funding of Expenditures:				
General Fund (01)	$202,134	$91,230	$93,511	$95,849
TOTAL Funding of Exp.	$202,134	$91,230	$93,511	$95,849
Revenues:				
General Fund (01)	($1,486,583)	($1,487,514)	($1,488,407)	($1,489,300)
Coal Bed Methane Account (02)	($20,267)	($20,280)	($20,292)	($20,304)
University System Levy Account (02)	($43,665)	($43,692)	($43,718)	($43,745)
Reclamation and Development Grant Fund	$1,538,850	$1,539,813	$1,540,737	$1,541,662
Orphan Share (02)	$1,538,850	$1,539,813	$1,540,737	$1,541,662
Local Governments	$55,479,109	$55,513,854	$55,547,163	$55,580,491
TOTAL Revenues	$57,006,294	$57,041,994	$57,076,220	$57,110,466
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($1,688,717)	($1,578,744)	($1,581,918)	($1,585,149)
State Special Revenue (02)	$3,013,768	$3,015,654	$3,017,464	$3,019,275
Local Governments	$55,479,109	$55,513,854	$55,547,163	$55,580,491

Effect on County or Other Local Revenues or Expenditures:

1. This legislation would increase revenues received by cities and counties by $55,479,109 in FY 2008, $55,513,854 in FY 2009, $55,547,163 in FY 2010, and $55,580,491 in FY 2011.

Technical Notes:

1. Page 7, line 15, the "s" at the end of "productions" should be removed.
2. The codification instructions indicate that this bill is intended to be codified in 15-31-101, MCA. Section 15-31-101, MCA, was repealed.
3. The effective date is July 1, 2007. The Department of Revenue requests that the effective date be moved back at least six months to develop and implement the computer systems and taxpayer instructions necessary to implement this legislation. The interim period of identifying tax that is to go to the counties will be difficult. It will require the operators to separately identify the production and value in this time period separately from the rest of the production and value to isolate and distribute the correct amount. Further, HB 598 states that the money get distributed to every county in the state (not just the oil and gas producing counties), thereby causing more programming and a whole different distribution scheme for these interim funds.
4. The meaning of "primary system" as it relates to roads is not clear.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*